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ANALYSIS OF AGENCY PROPOSALS FOR BUDGET REDUCTIONS, 1993 BIENNIUM

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A Report Prepared for the

Legislative Finance Committee

by

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SUMMARY

On August 12, the Office of Budget and Program Planning (OBPP) requested state agencies to identify $71.1 million in potential budget reductions, fund balance transfers, or other measures to address a projected $73 million shortfall in revenue for the 1993 biennium. As of September 3, agencies had identified $43.9 million in possible "budget balancers". The university system, legislative agencies, the Judiciary, Department of Justice, and two executive branch agencies have not yet provided specific budget reduction proposals.

In general, agencies proposed to hold positions vacant, reduce travel, and eliminate equipment purchases to meet the budget reduction "targets". However, only one-third ($15.1 million) of the agency proposals represent budget reductions in current, ongoing operations. Two-thirds ($28.8 million) of the proposals are to: 1) provide "one-time" savings through accounting changes, fund balance transfers, or increased revenue estimates; 2) reduce pass-through funds to local governments and schools; and 3) delay new programs, projects, or FTE authorized for the 1993 biennium.

Over one-half of the agency proposals may require legislative action. For example:

1) the Department of Corrections and Human Services proposes to close certain programs at Galen, effective January 1, 1992, for a projected $4.3 million savings during the biennium. Based on appropriation act language and statutes, the Legal Services Director of the Legislative Council concluded that this action would be contrary to existing law.

2) the department is also proposing to delay the construction of the Eastern Montana Veteran's Home and transfer the $2 million state match to the general fund. The bill passed by the 1991 legislature reappropriating

cigarette tax collections as the state match does not include a provision allowing unused funds to revert to the general fund.

3) the departments of Social and Rehabilitation Services and Family Services propose a "one-time" savings of $9.9 million by converting from an accrual method of accounting to a cash basis for Medicaid payments. Current law requires that all state financial transactions be recorded in accordance with generally accepted accounting principles (GAAP), and staff of the Office of the Legislative Auditor state that a cash basis is not allowed under GAAP. They also note that deferring recording of medicaid costs until paid will not increase the general fund balance, since all outstanding obligations must be disclosed in the state's annual financial statement.

4) a number of agencies propose to delay or eliminate budget modifications or miscellaneous appropriations approved by the 1991 legislature. Many of these budget modifications and all the miscellaneous appropriations are separate, "line-item" appropriations. A legal opinion issued by the Legal Services Director, Legislative Council, states that under current law the Governor can not reduce any appropriation by more than 15 percent.

Agencies say that some of the proposed reductions will result in lower state and federal revenue. The Department of Revenue proposes to reduce audit travel and leave vacant six new tax examiners and accounts receivable positions, which were projected to produce $4.7 million in additional revenue during the biennium. Several state agencies said that general fund reductions will reduce federal funds and may endanger agencies' "maintenance of effort" requirements.

It is important to note that these potential "budget balancers" are those identified by agencies. OBPP and the Governor have not yet announced their decisions concerning budget reductions.

To provide historical perspective on budget reductions in recent years, the report summarizes the gubernatorial and legislative actions taken to balance the state budget for fiscal 1986 and 1987.

OBPP REQUEST

On August 12, the Office of Budget and Program Planning (OBPP) sent a memo to all state agencies requesting assistance in planning for budget reductions in fiscal 1992 and fiscal 1993. The memo included a "target" budget reduction of 8 percent per year of the agency's total general fund appropriation. Agencies were asked to respond by August 21, identifying potential "budget balancers" in four areas:

1) general fund budget reductions;

2) unrestricted fund balances that could be transferred to the general fund without legislative action;

3) fund balances that could be transferred to the general fund with legislative action; and

4) measures that could be suggested to the 1993 legislature to reduce reliance on the general fund.

OBPP began meeting with agencies on August 26 to discuss the items identified in their responses. OBPP's memo stated: "it is the Governor's intention to announce major decisions in the neighborhood of September 6, 1991."

AGENCY RESPONSES

As of September 3, 31 agencies had responded, identifying $43.9 million in possible "budget balancers". This total is $27.2 million short of the $71.1 million target set by OBPP. Attachment A shows the 8 percent "target" OBPP calculated for each agency and the total budget reductions identified by each agency.

Several agencies have not yet identified potential areas of savings. The four directors of legislative agencies have all notified OBPP that their

committees will consider OBPP's budget reduction request at September meetings. Two agencies headed by elected officials--Judiciary and Justice--have responded, but not itemized specific budget reductions. Two executive branch agencies have not yet completed their written responses: Health and Environmental Sciences and the Governor's Office.

The university system, which had a "target" budget reduction of $21.0 million or 30 percent of the total proposed budget reduction, has not yet identified areas for budget reduction. At an August 22 meeting, the Board of Regents instructed the Commissioner of Higher Education staff to:

> A. Make all efforts to reach accommodation with the Governor's office over the budget recision issue.
>
> B. With the concurrence of the Board, initiate steps necessary to determine whether the laws of Montana require the Regents to revert previously appropriated funds upon the direction of the Governor.
>
> C. Explore the possibility of complying with budget cuts directed by the Governor so that in the event litigation results in a final decision adverse to the Regents, compliance can be attempted in the fashion least destructive to the integrity of Montana higher education.
>
> D. Concurrently explore the feasibility of making a good faith effort to share in solving any verified general fund deficit regardless of the results of any litigation undertaken by the Board.

While the Board of Public Education has identified potential budget reductions that would meet its "target", members voted on August 29 to request exemption from the cut for the Board and the School for the Deaf and Blind. The State Library Commission has requested exemption for state aid to local libraries and the State Library book budget. The Public Services Commission has requested exemption, since its general fund appropriation is paid by a tax on regulated industries. Any budget reduction results in a corresponding decrease in general fund revenue.

ANALYSIS OF PROPOSED REDUCTIONS

Following is an analysis of the budget reductions identified by agencies in their responses to OBPP. <u>It is important to note that these are the potential budget cuts identified by agencies. OBPP and the Governor</u>

have not yet announced their decisions concerning budget reductions. The Governor is, obviously, not required to accept these agency recommendations. Section 17-7-140, MCA, gives the Governor authority to reduce all appropriations (except those of the legislative and judicial branch, school foundation program and special education, salaries of elected officials, and principal and interest payments on state debt) by up to 15 percent. According to a 1986 Attorney General's opinion, the Governor's power to reduce appropriations extends to the budgets of agencies headed by elected officials. While the Board of Regent's Chief Legal Counsel has raised questions about the Governor's authority to reduce funds appropriated to the university system, this issue has not been referred to a court.

Reductions in Agency Operations

In order to meet the 8 percent annual targets, many agencies propose to leave positions vacant, cut staff travel and training, delay equipment purchases, and make other reductions in agency activities.

Only one agency (the School for the Deaf and Blind) said existing staff would need to be laid-off to meet the proposed budget reduction. Most agencies said that current vacancies would be maintained and normal turnover "managed" to ensure the necessary level of vacancy savings. However, several agencies warned that they might not be able to perform their statutory duties with this level of vacancies. For example, one of the Department of Revenue's options for budget reductions in the Property Assessment Division is based on the assumption that the legislature would provide an additional two year extension for the completion of reappraisal, extending the statutory date until December 31, 1994.

While most agencies did not indicate a specific percentage reduction in travel and equipment, a few agencies did. The Department of Natural

Resources and Conservation proposed to cut staff out-of-state travel by 90 percent and eliminate its entire general fund equipment budget. The Montana Arts Council proposes to reduce its in-state travel by 50 percent.

However, only one-third of the total "budget balancers" identified by state agencies represent budget reductions in current, ongoing operations. As Table 1 shows, agencies have proposed a number of actions that would: 1) provide "one-time" savings through accounting changes, fund balance transfers, or increases in revenue estimates; 2) reduce pass-through funds to local governments or schools; or 3) delay new programs, projects, or FTE authorized for the 1993 biennium. These proposals comprise two-thirds of the total "budget balancers" identified by agencies.

TABLE 1
Agency Proposals to Balance the Budget
1993 Biennium

	Total (Millions)
Fund Balance Transfers	$ 6.6
Medicaid Billing Change	9.9
Revenue Estimate Increases	4.5
Local Government/School Impact	2.5
Budget Modification/New Program Delay or Elimination	5.3
Total	$28.8

In their responses, agencies have expressed concern about the impact of the identified reductions. For example, the Department of Corrections and Human Services stated that:

> ...reducing the department's budget by $12 million this biennium would severely inhibit our ability to provide the minimum programs mandated by statute or required by certification standards and could have an even larger impact to the general fund. With this in mind, the department's proposals for this budget mitigation can best be accomplished by eliminating low priority, duplicated, or unneeded programs, delaying implementation of new programs, revising revenue projections..., and transferring unused special revenue account balances to the general fund.

The Department of Revenue stated:

> Our ability to address these issues is already exacerbated by [the] vacancy saving requirement. [This] requirement coupled with 8% general fund cuts reduces total departmental spending by a full 10%. A ten percent reduction now, combined with the budget reductions experienced over the past several years, will have a very dramatic impact on agency operations and consequently state revenues.

The department estimates that holding audit and collection positions vacant and reducing audit travel will reduce general fund and school equalization account revenues by $4.7 million during the 1993 biennium.

The State Library Commission wrote:

> ...a 2% reduction in general funding of operations is a workable reduction. Anything beyond this will severely impact the operation and will endanger other sources of funds which require certain matching of state general revenue.

Legal Issues Affecting Proposed Budget Reductions

Over half of the "budget balancers" proposed by agencies may require legislative action, as shown in Table 2 and discussed below. If no legislative action is taken until the 1993 session, the savings in some cases will be substantially less than shown in the agency response.

TABLE 2 "Budget Balancers" That May Require Legislative Action 1993 Biennium		
Agency	Item	Total (Millions)
Corrections & Human Services	Closure of Galen Programs	$4.3
	Transfer of Cigarette Tax (Veterans' Home)	2.0
Revenue	Delay Completion of Reappraisal Cycle	0.9
DNRC	Water Development Grants	0.2
	Defer Missouri EIS	0.1
SRS & DFS	Medicaid Billing Change	9.9
Commerce	Coal Board Fund Transfer	0.6
Various	Delay/Eliminate Budget Modifications	5.3
Total		$23.3

The Department of Corrections and Human Services proposes to eliminate the nursing home care and acute hospital care at the Galen campus of Montana State Hospital by January 1, 1992, for an estimated savings of $4.3 million during the 1993 biennium. It proposes to transfer current nursing home patients to other state facilities and private nursing homes, while continuing to provide inpatient chemical dependency services at Galen. Rejecting an executive proposal to close Galen, the 1991 legislature established a committee to study the current and potential uses of the campus and placed the following language in the House Bill 2:

> The department shall continue to provide acute hospital care, intermediate nursing care, and chemical dependency services at the Montana state hospital at Warm Springs and Galen without significant changes in the program at either campus.

Based on this language and statutory provisions, the Director of the Legal Services Division, Legislative Council, has issued an opinion (attached) stating that eliminating the hospital or intermediate nursing care programs would be contrary to existing statute. A local committee has

announced their intention of legally challenging any attempt to close the two programs.

Many agencies propose to delay or eliminate budget modifications approved by the 1991 legislature. However, this may run counter to existing law. Section 17-7-401, MCA, states that the Governor can reduce appropriations by up to 15 percent. Many of the budget modifications approved for the 1993 biennium are separate, "line-item" appropriations in House Bill 2. In a recent legal opinion, the Director of the Legal Services Division, Legislative Council, has concluded that each line-item is an "appropriation". He also stated:

> To construe "appropriation" to mean the total appropriation for an agency would allow the Governor to eliminate entire programs. Authorizing the Governor to eliminate entire programs would be tantamount to a line item veto outside the parameters of the [Montana constitution and statutes]. In light of the restrictive fiscal situation of the past several years, it is unlikely that agencies have implemented or received funding for discretionary programs. Therefore, the elimination of entire programs would in most instances conflict with specific statutory requirements...The only method of implementing section 17-7-140, MCA, to avoid these problems is for the Governor to reduce specific items by a permissible amount.

While the Governor may not be allowed to reduce "line-item" appropriations by more than 15 percent, no statute prohibits him from establishing reversion "targets" for agencies in excess of this amount. Directors can then make management decisions in meeting these targets, eliminating or delaying new programs if necessary to meet these targets. Constraints on these management decisions include ensuring that statutory duties are performed and that program transfers to reallocate resources do not exceed the limits imposed in House Bill 2. However, under current law, the Governor has no authority to enforce reversion "targets" for non-executive branch agencies or agencies headed by elected officials.

Fund Balance Transfers

At OBPP's request, agencies identified $6.6 million in fund balances that could be transferred to the general fund. Table 3 shows the source of the recommended transfers.

TABLE 3
Fund Balances Suggested for Transfer to General Fund

Dept.	Item	1993 Biennium Total
SRS	Child Support Enforcement	$ 500,000
	Unreconciled Balance	1,000,000
Human Services/Corrections	Prison Ranch	605,212
	Eastern Montana Vets Home	1,991,897
State Lands	Timber Standing Improvement	120,000
Secretary of State	Administrative Code	20,000
	Records Management	20,000
Revenue	Liquor Funds	1,000,000
Administration	Internal Service Funds	192,000
	Interest on Social Security	138,964
Military Affairs	Transfer State Fund Acct.	183,431
Commerce	Coal Board	600,000
DNRC	Water Development Grants	277,532
Total		$6,649,036

Approximately half of the recommended transfers require legislative action:

1) Eastern Montana Veteran's Home (EMV). The Department of Corrections and Human Services proposed to delay construction of the EMV in Glendive for another biennium and transfer the $2.0 million in cigarette tax that was collected as state match for the project to the general fund. The bill passed by 1991 legislature reappropriating the cigarette tax collections for this purpose contains no provision for reversion of unused funds to the general fund.

2) Coal Board Transfer. The Department of Commerce proposes that the entire 8 percent "target" for the agency be met by reducing Coal Board grants to local governments impacted by coal development. It recommends that $300,000 per year of the approximately $2.5 million statutorily allocated to the Coal Board's local impact account be transferred to the general fund. Section 90-6-207(6), MCA, provides: "All funds placed in the local impact account...shall be subject to appropriations by the legislature for use related to local impact." Section 90-6-212(3), MCA, states: "The unexpended balance in the local impact account at the end of each biennium must be deposited to the credit of the state special revenue fund for state equalization aid to public schools of the state."

3) Water Development and Reclamation and Development Grants. The Department of Natural Resources and Conservation has identified $277,532 of grants that were appropriated for funding by the legislature prior to 1988 which are either not yet contracted for or the contract has expired. Legislative action would be necessary to transfer these funds into the general fund.

Some of the other transfers may require the agency to seek a general fund loan in order to operate the program funded from the account. For example, SRS maintains a proprietary fund balance of up to $500,000 for cash flow purposes in its Child Support Enforcement program. It proposes

to transfer the entire balance to the general fund and use short term loans from the general fund until the proprietary fund cash flow is sufficient to operate the program. The Department of Corrections and Human Services proposed to transfer $605,212 from the prison ranch revolving account at the end of the 1993 biennium, but notes that agricultural conditions and prices may affect the operating costs of the program.

Medicaid Billing Change

SRS has proposed that it and Family Services realize a "one-time" savings of $9.9 million in fiscal 1992 by converting from the current modified accrual accounting system for Medicaid expenditure to a cash accounting method.

Attached is an LFA staff memo analyzing the impact of this proposal. Based on consultation with staff of the Office of Legislative Auditor, LFA staff concluded the proposal:

1) would not cut costs; it would simply defer recording of these costs until the next fiscal year;

2) would not result in an increase in the general fund balance, since generally accepted accounting principles (GAAP) require that all outstanding obligations be shown in the annual official statement of the state's financial position; and

3) would require legislative action for implementation, since GAAP does not allow cash accounting and current law requires that all state financial transactions be recorded "in accordance with generally accepted accounting principles."

Delay or Eliminate New Programs

Agencies propose the delay or elimination of $5.3 million of the $63.7 million of budget modifications and miscellaneous ("cat and dog") bills approved by the 1991 legislature. Following are some proposals:

Department of Family Services

--design the management information system in-house, saving $313,694 of the $547,339 appropriated in House Bill 569.

--reduce the funds appropriated in House Bill 371 for in-home aging services and in House Bill 491 for foster care respite care by 50 percent ($150,000).

--revert $549,919 of the budget modification for continuum of care services.

Department of State Lands

--eliminate $250,000 of the $300,000 Trust Land Access budget modification by not undertaking an economic analysis of recreational land.

Department of Corrections and Human Services

--delay implementation of pre-release expansions, house arrest program, intensive supervision program, local jurisdiction sentencing, and hiring of three additional parole and probation officers until fiscal 1993.

--eliminate modification for medical consultant to provide medical policy guidance and direction to the department and institutions.

Department of Revenue

--eliminate hiring three tax examiners, added in the House Bill 2 free conference committee on the assumption they would generate $1.5 million of additional revenue during the biennium.

--eliminate three accounts receivable staff added by budget modification; $2.6 million was added to the HJR 24 revenue estimate resolution based on anticipated collections from these new staff.

Department of Administration

--eliminate general fund support of the Montana State University engineering complex project.

--delay construction of bonded projects (men's prison expansion, women's prison construction, university buildings) or structure the debt to defer interest payments until the 1995 biennium.

--reduce funding by $600,000 for the university system's deferred maintenance and equipment projects.

Department of Labor and Industry

--eliminate the additional human rights investigator added by budget modification.

Impact on Local Governments and Schools

As Table 4 shows, $2.5 million of the budget cuts proposed by state agencies would reduce funds passed through to local governments and schools. For example, the Department of Revenue proposes to reduce the state contribution for county assessors' and deputies' salaries from approximately 70 percent to 64 percent, effective in fiscal 1992. It notes that counties may have difficulty in absorbing this increased cost, since fiscal 1992 mill levies have already been set. SRS suggests that counties which run their own welfare programs (non-assumed counties) pay their computer costs for the TEAMS project. The Department of Corrections and Human Services proposes to start billing counties for court-ordered psychiatric examinations. While counties can seek reimbursement for this

new expense from the District Court Criminal Reimbursement program administered by the Montana Supreme Court, use of the program's funds for this purpose will reduce funds available for grants to district courts.

TABLE 4
Impact of Budget Reductions on Local Governments and Schools, 1993 Biennium

Dept.	Item	
SRS	Non-assumed County Computer Processing	$300,000
Human Services/Corrections	Court-ordered Evaluations	913,090
State Lands	Equalization Payments	42,400
Commerce	Coal Board Grants	600,000
Revenue	County Assessors Salaries	278,896
Highway Traffic Safety	DUI Fees Paid to Counties	31,840
OPI	Gifted and Talented	48,000
	Secondary Vo-ed	72,000
	Adult Basic Education	40,000
Administration	County Tax Appeal Boards	105,312
DNRC	Water Development Grants	47,500
Total		$2,479,038

Increased Revenue Estimates

As Table 5 shows, four agencies have revised their revenue estimates for federal and private funds upward, resulting in increased revenue to the general fund or decreased general fund costs.

TABLE 5 Revenue Estimate Increase 1993 Biennium		
Agency	Source	Total
Family Services	Parental Contribution for Inpatient Psychiatric	$928,792
	Increased IV-B Federal Funds	150,000
	Daycare Block Grant	623,554
	Misc. Federal Funds	747,820
Corrections & Human Services	Increased Medicaid and Private Pay Reimbursement	584,445
	Medicaid Cost Settlement	1,094,664
	Increased V.A. Per Diem	290,682
State Lands	Increased Tree Seedling Prices	70,000
Agriculture	Federal Indirect Costs	40,000
Total		$4,529,957

Department of Family Services

The department proposes to reduce state matching costs for Medicaid payments for inpatient psychiatric services for youth by implementing a rule change requiring parental assets to be considered. SRS proposed a similar rule in the 1991 biennium after a report to the Legislative Finance Committee raised the issue, but the proposed rule was not adopted due, in part, to industry concerns.

The department plans to fund daycare provider rate increases with federal block grant funds (approved by the 1991 legislature if federal regulations allowed). It also anticipates increased federal funding due to pending federal legislation, allowing the reduction of general fund costs.

Department of Corrections and Human Services

The department estimates that an additional $1.2 million in reimbursement for patients in state institutions will be realized due to increased per diem rates, updated patient day figures, increased medicaid eligibility, and private pay revenue factors. However, it notes that the proposed closure of Galen programs on January 1, 1992, would reduce reimbursements by $0.6 million, for a net revenue gain of $0.6 million. It calculates that Veterans' Administration per diem rate increases will produce $0.3 million more than estimated during the legislature.

It also anticipates that medicaid cost settlements for underpayment at three state facilities will result in $1.1 million more being deposited in the general fund than was anticipated by the legislature.

Department of State Lands

The department proposes to increase the price it charges for tree seedlings and use the anticipated $70,000 to offset general fund costs.

Department of Natural Resources and Conservation

While DNRC did not include the following two proposals in its summary of budget reductions, it suggested a series of "mitigations" OBPP might consider to reduce the impact of the budget cuts on the agency. Two of the proposed mitigations are doubling the grazing fee charged to grazing districts and changing the water rights fee structure to double revenue collections. These proposals, which would increase fiscal 1993 revenue by $86,000, are not included in the table above.

Reduced Federal Funds

Several agencies have noted that reducing general fund appropriations will reduce federal funding, due to funding formulas or maintenance of effort requirements.

The Office of Public Instruction (OPI) states that each $1 cut in Adult Basic Education program results in the loss of $3 in federal funds. It also notes that reductions in general fund support for the school lunch program may violate federal matching requirements, endangering $4 million in federal funds.

The State Library notes that federal laws require the state contribution for certain programs to remain at least at the level in the second preceding fiscal year. It warns that cuts below this level could endanger over $660,000 in federal funds.

The Montana School for the Deaf and Blind says the proposed cuts will result in the loss of $69,000 in federal funds.

RECENT BUDGET REDUCTIONS

To provide some historical perspective on budget reductions in recent years, following is information on the budget reductions imposed in fiscal 1986-7.

Fiscal 1986

Evidence of revenue shortfalls began appearing soon after the 1985 legislature adjourned. The impact of the drought on income tax collections combined with falling oil prices and interest rates reduced fiscal 1986 general fund revenues by almost 10 percent. In January 1986, the Governor imposed a 2 percent general fund reduction for the fiscal year,

reducing appropriations by $7.0 million. The general fund balance at the end of the fiscal year was $16.0 million, rather than the $39.2 million anticipated when the 1985 legislature adjourned.

Fiscal 1987

In June 1986 the legislature met in special session to balance the fiscal 1987 budget. Anticipated revenues for fiscal 1987 were 15 percent less than estimated by the 1985 legislature, due to continuing income tax collection shortfalls and low oil prices and interest rates. The Executive Budget recommended a combination of proposals totalling $93.0 million to reduce expenditures, appropriate cash balances, redirect funds, and increase revenues. These proposals included a 5 percent cut in state agencies' budgets (with the exception of most SRS benefits and direct care at state institutions) and elimination of the fiscal 1987 pay plan increase. Attached is the Executive Budget summary of these proposals.

While the legislature adopted most of the proposals, it: 1) provided a 1 percent increase in school foundation schedules; 2) declined to close the Youth Evaluation and "Lighthouse" programs; 3) increased gasoline taxes by 2¢ per gallon rather than 5¢ per gallon for gasoline and 3¢ per gallon for diesel as recommended by the Executive Budget.

Because unions would not agree to amend collective bargaining agreements to reflect the wage freeze adopted by the legislature, the fiscal 1987 pay increase went into effect. Since funding for the increase was eliminated during the 1986 special session, agencies had to absorb the pay plan costs ($8.1 million general fund or slightly over 2 percent of total budgets). After the legislature adjourned in early July, revenues continued to fall. In November 1986, the Governor imposed an additional 2 percent across-the-board reduction on agency budgets. In total, some agencies'

fiscal 1987 budgets were reduced almost 9 percent from the level approved by the 1985 legislature.

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Attachment A

Agency Budget Reduction
Targets and Recomendations

AGENCY	TARGET REDUCTION		AGENCY OFFERINGS		BIENNIAL		
	FY 1992	FY 1993	FY 1992	FY 1993	TARGET	OFFERING	DIFFERENCE
LEGISLATIVE AUDITOR	$101,785	$104,104	$0	$0	$205,889	$0	($205,889
LEGISLATIVE FISCAL ANALYST	76,800	73,808	0	0	150,608	0	(150,608
LEGISLATIVE COUNCIL	176,503	173,772	0	0	350,275	0	(350,275
ENVIRONMENTAL QUALITY COUNCIL	23,779	24,151	0	0	47,930	0	(47,930
JUDICIARY	680,107	677,610	0	0	1,357,717	0	(1,357,717
GOVERNOR'S OFFICE	214,867	206,176	0	0	421,043	0	(421,043
SECRETARY OF STATE'S OFFICE	85,109	81,120	70,000	25,000	166,229	95,000	(71,229
COMMISSIONER OF POL. PRACTICES	14,007	9,766	11,886	11,887	23,773	23,773	0
STATE AUDITOR'S OFFICE	192,411	184,276	77,000	77,000	376,687	154,000	(222,687
OFFICE OF PUBLIC INSTRUCTION	1,260,693	909,421	419,850	409,350	2,170,114	829,200	(1,340,914
CRIME CONTROL DIVISION	40,547	42,973	40,574	42,973	83,520	83,520	0
HIGHWAY TRAFFIC SAFETY	15,920	15,920	15,920	15,920	31,840	31,840	0
DEPARTMENT OF JUSTICE	1,020,637	1,060,990	0	0	2,081,627	0	(2,081,627
PUBLIC SERVICE REGULATION	174,335	166,537	0	0	340,872	0	(340,872
BOARD OF PUBLIC EDUCATION	9,761	9,543	9,761	9,543	19,304	19,304	0
COMMISSIONER OF HIGHER ED.	10,427,151	10,549,259	0	0	20,976,410	0	(20,976,410
SCHOOL FOR THE DEAF & BLIND	220,836	224,402	221,598	229,517	445,238	451,115	5,877
MONTANA ARTS COUNCIL	11,465	10,242	11,534	10,173	21,707	21,707	0
LIBRARY COMMISSION	103,973	85,202	13,051	12,710	189,175	25,761	(163,414
HISTORICAL SOCIETY	106,562	105,904	106,562	108,191	212,466	214,753	2,287
DEPT OF FISH, WILDLIFE, & PARKS	34,459	34,837	34,459	34,837	69,296	69,296	0
DEPT HEALTH & ENVIRONMENTAL SCI.	384,680	303,116	0	0	687,796	0	(687,796
DEPARTMENT OF TRANSPORTATION	75,414	49,993	75,414	49,993	125,407	125,407	0
DEPARTMENT OF STATE LANDS	741,281	728,067	738,774	456,363	1,469,348	1,195,137	(274,211
DEPARTMENT OF LIVESTOCK	65,147	66,582	65,000	20,000	131,729	85,000	(46,729
DEPT OF NATURAL RESOUCES & CON.	390,118	394,056	392,688	391,486	784,174	784,174	0
DEPARTMENT OF REVENUE	1,677,952	1,647,059	1,677,974	1,647,047	3,325,011	3,325,021	10
DEPARTMENT OF ADMINISTRATION	550,101	313,243	1,734,478	1,216,212	863,344	2,950,690	2,087,346
DEPARTMENT OF AGRICULTURE	99,929	89,634	99,930	89,634	189,563	189,564	1
DEPT OF CORRECTIONS & HUMAN SER.	5,968,635	5,946,261	6,532,263	4,766,356	11,914,896	11,298,619	(616,277
DEPARTMENT OF COMMERCE	294,810	230,933	300,000	300,000	525,743	600,000	74,257
LABOR & INDUSTRY	62,559	61,045	62,550	61,045	123,604	123,595	(9
MILITARY AFFAIRS	183,431	170,324	183,431	170,325	353,755	353,756	1
DEPT OF SOCIAL & REHAB. SER.	7,597,609	8,238,167	12,455,000	3,380,766	15,835,776	15,835,766	(10
DEPARTMENT OF FAMILY SERVICES	2,508,439	2,501,586	2,508,439	2,501,586	5,010,025	5,010,025	0
TOTAL	$35,591,812	$35,490,079	$27,858,136	$16,037,914	$71,081,891	$43,896,050	($27,185,841

09/03/91
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ATTACHMENT B

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August 27, 1991

Representative William "Red" Menahan
1304 W. 5th Street
Anaconda, Montana 59711

Dear Representative Menahan:

I am writing in response to your request for information as to whether the administration may close programs at the Galen campus of the Montana State Hospital pursuant to the authority contained in House Bill No. 454. House Bill No. 454 was enacted as Chapter 787, Laws of 1991. Chapter 787, Laws of 1991, codified conditions for appropriations usually contained in each general appropriations act. Section 10, Chapter 787, Laws of 1991, was codified as section 17-7-140, MCA. Section 17-7-140, MCA, provides:

> **Reduction of appropriation.** (1) Except as provided in subsection (2), in the event of a shortfall in revenue, the governor may reduce appropriations. An appropriation may not be reduced by more than 15%.
>
> (2) The appropriations for the following may not be reduced:
> (a) payment of interest and principal on state debt;
> (b) the legislative branch;
> (c) the judicial branch;
> (d) the school foundation program, including special education; and
> (e) salaries of elected officials during their terms of office.

In an August 21, 1991, letter to Teresa O. Cohea, Legislative Fiscal Analyst, I concluded that:

> "appropriation" within the context of section 17-7-140, MCA, means the money designated for each special purpose, i.e., "line item". To construe "appropriation" to mean the total appropriation for an agency would allow the Governor to eliminate entire programs. Authorizing the Governor to eliminate entire programs would be tantamount to a line item veto outside of the parameters of Article VI, section 10, of the Montana Constitution, as implemented by section 5-4-303, MCA. In light of the restrictive fiscal situation of the past several years, it is unlikely that agencies have implemented or received funding for discretionary programs. Therefore, the

elimination of entire programs would in most instances conflict with specific statutory requirements imposing a duty on an agency to carry out a function. The only method of implementing section 17-7-140, MCA, to avoid these problems is for the Governor to reduce specific items by a permissible amount.

The specific statutes governing Galen are as follows:

53-6-301. Location and primary function of hospital. (1) The agency providing comprehensive health care services at Galen and Warm Springs, Montana, is the Montana state hospital and as its primary function provides:

(a) care and treatment of mentally ill persons;

(b) diagnosis, care, evaluation, treatment, referral, and rehabilitation of persons afflicted with chemical dependency;

(c) care and treatment of institutional residents or clients of the department's community and residential programs who require acute hospital care or nursing care;

(d) treatment of tuberculosis and silicosis (commonly called miner's consumption);

(e) detoxification of those persons who seek relief from the disabling effects of alcohol and other chemical substances; and

(f) contingent upon space and funds, the treatment of pulmonary diseases and other medical or organic disorders.

(2) The campus facility at Warm Springs, Montana, is the component designated as the mental health facility, as defined in 53-21-102, of the department of corrections and human services for the care and treatment of mentally ill persons.

(3) The designated campus facilities at Galen, Montana, are the components designated as the department's residential treatment facilities for those persons suffering from chemical dependency.

(4) The campus facility at Galen, Montana, licensed to provide acute hospital and intermediate nursing care, is the facility component designated for the care and treatment of the medical and organic disorders described in this section. (emphasis added)

53-6-303. Transfer of patients from Galen to mental institution. A mentally retarded or mentally ill person residing at the Galen campus facility of the Montana state hospital may be transferred to the Warm Springs campus facility of the Montana state hospital, the Montana center for the aged, or the Montana developmental center with the approval of the department of corrections and human services if the department determines that the transfer will be in the best interests of the patient. Unless a medical or psychiatric emergency exists, 15 days prior to the transfer the department shall send notice of the proposed transfer to the patient's parent, guardian,

or spouse or, if none is known, his nearest relative or friend. In the case of an emergency transfer, the department shall send notice within 72 hours after the time of transfer.

53-6-304. Alcoholic treatment center. (1) There is an alcoholic treatment center located at the Montana state hospital. The admittance and discharge procedures for alcoholics are the same as for ill persons.

(2) As used in this section:

(a) "alcoholism" means a chronic illness or disorder of behavior characterized by repeated drinking of alcoholic beverages to an extent which endangers the drinker's health, interpersonal relations, or economic functioning or to an extent which endangers the public health, welfare, or safety;

(b) an "alcoholic" is a person suffering from the illness of alcoholism.

(3) The alcoholic treatment center shall provide care, evaluation, treatment, referral, and rehabilitation to persons in Montana who are referred for the treatment of the illness of alcoholism or the complications thereof.

In addition to the statutes cited above, the narrative portion of House Bill No. 2, the general appropriations bill, contained the following language on page D-11:

Transfers may be made between line items within the mental health division and the alcohol and drug abuse division (chemical dependency) for the purpose of accurately allocating operating expenses associated with the alcohol and drug programs on the Galen campus upon approval of the governor or his designated representative.

Included in item 3 are $22,492,426 in fiscal 1992 and $22,717,860 in fiscal 1993 for the operation of Montana state hospital. Except for approved transfers to the chemical dependency division for the purpose of accurately allocating operating expenses associated with the alcohol and drug programs on the Galen campus, no more than 5% of these funds may be transferred.... Included in the appropriation for the Montana state hospital chemical dependency program within item 4 are $1,408,733 in fiscal 1992 and $1,413,201 in fiscal 1993 for the operation of the Galen chemical dependency program. No more than 5% of these funds may be transferred.

The department shall continue to provide acute hospital care, intermediate nursing care, and chemical dependency services at the Montana state hospital at Warm Springs and Galen without significant changes in the program at either campus.

Article V, section 11(4), of the Montana Constitution requires that:

> (4) A general appropriation bill shall contain only appropriations for the ordinary expenses of the legislative, executive, and judicial branches, for interest on the public debt, and for public schools. Every other appropriation shall be made by separate bill, containing but one subject.

In 1975, the Montana Supreme Court construed this provision of the Constitution in determining whether conditions contained in the general appropriations act were properly applicable to the Board of Regents. The court in Board of Regents v. Judge, 168 Mont. 433, 543 P.2d 1323 (1975), stated:

> However, the legislature cannot do indirectly through the means of line item appropriations and conditions what is impermissible for it to do directly. Line item appropriations become constitutionally impermissible when the authority of the Regents to supervise, coordinate, manage and control the university system is infringed by legislative control over expenditures. On their face, the budget items and corresponding line items of H.B. 271 are reasonably related to the purpose of providing funds for necessary services and the other responsibilities of the legislature enumerated above. Judge at 450.

The court went on to determine that the conditioning of appropriations by the Legislature were proper exercises of the Legislature's appropriation power to the extent that the conditions did not infringe on the constitutional powers granted the regents. The court determined that the conditions would have to be individually scrutinized to determine their propriety. Judge at 451.

In City of Helena v. Omholt, 155 Mont. 212, 468 P.2d 764 (1970), provisions in an appropriation bill were found to be unconstitutional when conditions contained in the appropriation bill nullified and defeated the specific statute the appropriation was designed to implement. The court noted that the section of the bill containing conditions on the appropriation could not have been vetoed by the Governor and that his only alternative was to veto the entire bill and still fund the mandatory payments as required by statute. Omholt at 221-222.

In State ex rel. Davidson v. Ford, 115 Mont. 165, 141 P.2d 373 (1943), a case challenging conditions contained in an appropriation bill, the Montana Supreme Court determined that so long as the provisions of an appropriation bill are germane to the purpose of the appropriation, it does not conflict with any constitutional provision. The Court quoted from the New Mexico Supreme Court's decision in State ex rel. Lucero v. Marron, 17 N.M. 304, 128 P. 485 (1912), as follows:

> To sustain the contention that the general appropriation bill should contain nothing, save the bare appropriations of money, and that provisions for the

> expenditure of the money, or its accounting, could not be included therein, * * * would lead to results so incongruous that it must be presumed that the framers of the Constitution had no such intent in the adoption of the restrictions referred to. . . . When an appropriation is made, why should not there be included with such appropriation matter germane thereto and directly connected with it, such as provisions for the expenditure and accounting for the money, * * *. What valid objection can be interposed to such a course, so long as the Legislature confines the incidental provisions to the main fact of the appropriation, and does not attempt to incorporate in such act general legislation, not necessarily or directly connected with the appropriation legally made, under the restrictions of the section in question? Ford at 172.

The Attorney General has determined that when the restrictions in an appropriation bill clearly conflict with substantive statutory obligations, the substantive statutory obligation controls. 39 A.G. Op. 25 (1981). The language contained in the narrative to House Bill No. 2, the general appropriations bill of 1991, is not in conflict with section 53-6-301, MCA, but appears to be reasonably germane to the purpose of the appropriation. The language merely states that section 53-6-301, MCA, must be implemented. If the administration were to implement the appropriation reduction authority contained in section 17-7-140, MCA, by eliminating either the residential chemical dependency treatment component or the hospital and intermediate nursing care component for the care and treatment of medical and organic disorders at the Galen campus, the action would be contrary to the provisions of section 53-6-301, MCA.

It is important to also note that the Legislature enacted Chapter 546, Laws of 1991, establishing a committee to conduct a study of the past, current, and potential future uses of Montana State Hospital. The committee is a joint legislative/executive committee that is required to report its findings and conclusions, including a detailed listing of all options for the current and continued use of Montana State Hospital.

If you have any questions or if I can provide any additional information, please feel free to contact me.

Sincerely,

Gregory J. Petesch, Director
Legal Services Division

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ATTACHMENT C

STATE OF MONTANA

Office of the Legislative Fiscal Analyst

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HELENA, MONTANA 59620
406/444-2986

TERESA OLCOTT COHEA
LEGISLATIVE FISCAL ANALYST

September 5, 1991

TO: Legislative Finance Committee

FROM: Carroll South
Senior Fiscal Analyst

RE: Medicaid Accruals

As part of its response to the Governor's request to reduce general fund expenditures by 8 percent, the Department of Social and Rehabilitation Services (SRS) is recommending that beginning in fiscal 1992, certain medicaid expenditures be recorded on a "cash" basis, rather than the "accrual" system currently used. SRS suggests that 1992 general fund medicaid appropriations could be reduced significantly if this accounting change were made. Differences between cash and accrual accounting methods are discussed below.

ACCRUAL ACCOUNTING

Under generally accepted accounting principles (GAAP), funds needed to meet valid obligations remaining at fiscal year end must be accrued as expenditures. For example, if a service has been provided to a state agency prior to fiscal year end, a valid obligation exists and funds sufficient to pay for the service must be accrued (obligated), even if the agency has not been billed for the service by the time the state's "books" are closed. The amount accrued will appear as an expenditure against the

appropriation for the fiscal year in which the service was rendered, rather than the next fiscal year when the payment is actually made.

CASH ACCOUNTING

A cash accounting system records expenditures when they are actually paid, regardless of when the service or product being purchased was provided. For example, if a service has been provided to a state agency during one fiscal year but the bill has not been paid by fiscal year end, the expenditure would be recorded against the next year's appropriation when the payment is actually made. According to staff of the Office of the Legislative Auditor (OLA), using a cash accounting system is not acceptable under GAAP.

REASONS FOR THE SRS RECOMMENDATION

SRS's written response to the Governor's budget reduction request suggests that the state's accrual accounting system when applied to the medicaid program is flawed because:

> 1) There is no mechanism available to determine by fiscal year end which medical services provided during the year will ultimately be paid by medicaid. The existence of other third party payers, non-covered services, denial of payment, and ineligibility for services are justifications for not reimbursing a medicaid claim sent by a provider. Until it determines that a claim is appropriate, SRS argues that a valid obligation does not exist.
>
> 2) Current state law requiring use of the accrual accounting system results in inaccurate and ineffective medicaid reports, while switching to a cash accounting system would provide more current information to project future medicaid expenditures.
>
> 3) Using an accrual accounting system for medicaid expenditures causes problems in administering the program and can actually force SRS to violate GAAP in certain instances. If the final amount of legitimate medicaid charges exceed funds appropriated that year, payment must be delayed until the legislature convenes to appropriate additional funding, the payment is denied, or

payment is made from current year appropriations (which is a violation of GAAP).

4) Other states within the region, including Idaho, North and South Dakota and Wyoming operate their medicaid programs on a cash basis.

ACCRUAL AMOUNTS

Due to rapidly increasing medicaid expenditures, the actual dollar amount accrued at fiscal year end for medicaid services delivered during the year is becoming significant. The table below shows total projected fiscal 1992 medicaid expenditures for primary care, the amount estimated to be paid by fiscal year end, and the amount which would be accrued under current law.

Fiscal 1992 Estimated Primary Care Medicaid Expenditures/Accruals

Medicaid Service Type	$ Paid By 6/30/92	$ Paid By 6/30/94	Amount Accrued	% Paid By 6/30/92
Inpatient Hospital	$ 41,583,146	$58,919,480	$17,336,334	70.58%
Inpatient Psychiatric	6,196,957	8,405,918	2,208,961	73.72%
Residential Psychiatric	2,091,826	2,297,632	205,806	91.04%
Outpatient Hospital	10,679,388	13,205,486	2,526,098	80.87%
Physicians	18,776,944	23,725,727	4,948,783	79.14%
Other Practitioners	2,975,272	3,488,940	513,668	85.28%
Drugs	13,919,055	15,689,614	1,770,559	88.72%
Dental	3,271,812	3,681,393	409,581	88.87%
Other	15,674,892	20,520,555	4,845,663	76.39%
Totals	$115,169,293	$149,934,745	$34,765,452	76.81%

The table shows that $34.77 million (of which $9.84 million is general fund) will be accrued at the end of fiscal 1992 if current projections are accurate. The percentage of total valid obligations paid by fiscal year end varies significantly by service type, ranging from 70.6 percent for inpatient hospital services to 88.9 percent for dental services. While SRS continues to pay fiscal 1992 claims through fiscal 1994, approximately 99.0 percent of fiscal 1992 claims will be paid by the end of fiscal 1993.

Beginning in fiscal 1992, the general fund medicaid match for inpatient psychiatric services is appropriated to the Department of Family Services (DFS). Approximately $500,000 of the DFS general fund medicaid appropriation will be accrued at the end of fiscal 1992.

WOULD SWITCHING TO A CASH SYSTEM SAVE MONEY?

If the state began paying primary care medicaid charges on a cash, rather than accrual basis, the fiscal 1992 appropriation for primary care could, theoretically, be reduced by the amount shown in the accrued column of the above table ($34.77 million total, $9.84 million general fund). The amounts which are currently accrued would be paid from the fiscal 1993 appropriation. The same process would occur in fiscal 1983 and beyond. The last bill actually paid before fiscal year end would be the last expenditure recorded against that year's appropriation.

In practice, however, changing the way medicaid expenditures are recorded would save nothing. Reducing appropriations in entitlement programs such as medicaid and welfare will not reduce the cost. Only actions such as tightening eligibility and/or reducing service levels will reduce entitlement program costs. Recording medicaid expenditures on a "cash" basis as recommended by SRS simply postpones recording the liability for a valid obligation.

In addition, reducing the general fund medicaid appropriation by the amount of the valid obligation remaining at year end would have no impact on the general fund ending balance and would not contribute towards "balancing" the state budget, according to OLA staff. The state prepares a yearly financial statement, the Montana Comprehensive Annual Financial Report, which provides the official statement of Montana's financial condition

and its unobligated ending fund balances. The statement is audited by the Legislative Auditor to ensure that the financial information contained in the document accurately and fairly presents the financial position of the state. If the medicaid obligation remaining at year end were not covered by an expenditure "accrual" on the state's accounting system as is currently done, OLA staff state that it would have to be subtracted from the general fund balance shown in the comprehensive financial statement. Therefore, the unreserved general fund balance would not be increased if medicaid expenditures were recorded on a "cash" basis.

DOES CURRENT LAW PERMIT CASH ACCOUNTING?

Current law does not permit state agencies to record financial transactions on a "cash" basis. In order for SRS's recommendation to be implemented, the legislature would have to amend current law which requires that all financial transactions be recorded in "accordance with generally accepted accounting principles" (Section 17-1-102, MCA). However, as discussed earlier, amending the law to permit the recording of medicaid financial transactions in violation of GAAP would not save general fund monies, but could complicate the state's financial statement by requiring an "official" explanation of why the medicaid obligation remains unrecorded at year end.

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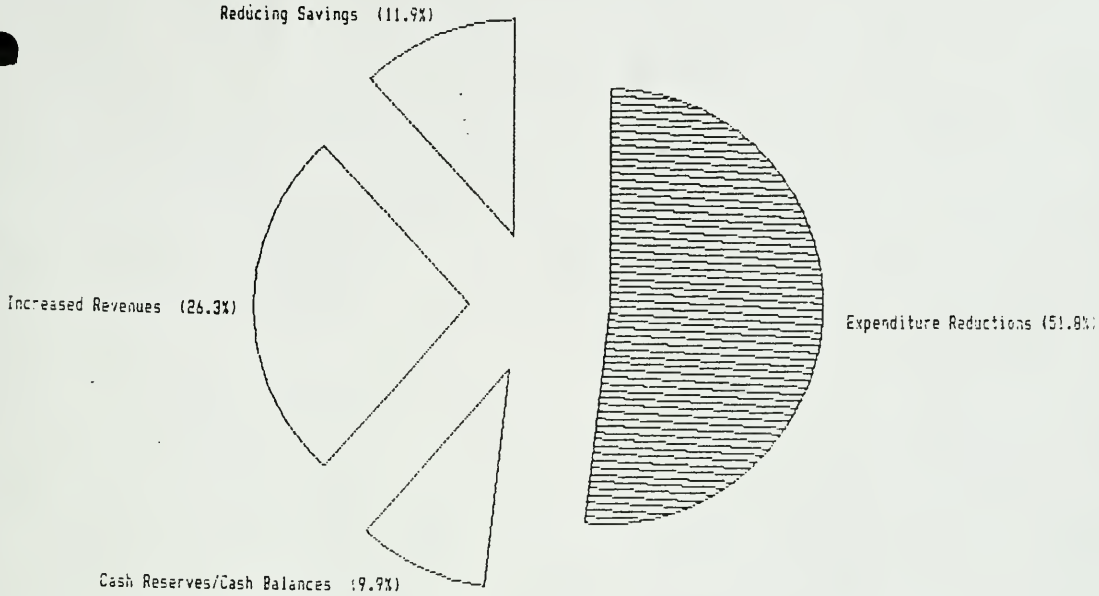
GOVERNOR'S EXECUTIVE BUDGET



GOVERNOR'S EXECUTIVE BUDGET

	Amount (in million $)	Percent
Expenditure Reductions	48.221	51.8%
Cash Reserves/Cash Balances	9.243	9.9%
Increased Revenues	24.475	26.3%
Reducing Savings	11.106	11.9%
Total	$93.045	